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SUBJECT: TAKING ADVANTAGE OF EU EXPANSION: SPANISH PRIVATE  
SECTOR MUSING

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1. SUMMARY. In a recent report, Spain's largest employers' organization, the Confederacion Espanola de Organizaciones Empresariales (CEOE), highlighted the challenges and opportunities for Spain presented by EU enlargement. Opportunities include potential for increased trade and investment, while challenges center on strategies to offset the competitive advantages of candidate countries, ranging from lower wages to weaker regulations. The CEOE study proposed an action plan that Spanish businesses from various sectors of Spain's economy could implement in order to face these challenges. The report holds that enlargement will only have a plus or minus 0.3% effect on Spain's GDP. Whether the impact is positive or negative will depend on the seriousness of the business community's efforts to prepare for the challenges of enlargement. END SUMMARY

2. CEOE, Spain's largest employers' organization, recently published a report that analyzes the implications of European enlargement for the Spanish private sector. In addition to touching upon general themes such as what the EU-15 and candidate countries need to do to guarantee a smooth and successful integration, the report addresses reforms that Spanish companies should introduce to take advantage of enlargement, and makes recommendations for dealing with the upcoming challenges. Bottom line, CEOE believes that the Spanish economy could avoid the negative impacts of EU enlargement if the Spanish business community prepares well. Contrary to many predictions, the CEOE report puts the economic effect of expansion at a small plus or minus 0.3% of Spain's GDP, but whether Spain's economy gains or loses depends on the efforts of Spanish businesses.

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CHALLENGES  
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3. Despite new business opportunities, there are challenges for the Spanish economy. The competitive advantages of the acceding countries will attract foreign investment away from Spain and increase competition with Spanish products. Competitive advantages are not limited to lower wages, but also include lower non-tariff trade barriers, higher fiscal incentives, and, at least temporarily, unfair government subsidies that are deemed by CEOE contrary to EU regulations. Lower standards for environmental protection, food safety, consumer protection, work environment, intellectual and industrial property protection, and trade and labor laws also lower business costs.

4. Additionally, Spain will lose EU cohesion funds after EU expansion. Currently, Spain is the biggest net beneficiary of EU funds. Spain received in absolute terms some 8 billion Euros last year (\$9.6 billion at a rate of EUR 1=USD 1.21). As EU funds are directed to new members, the Spanish government will have to take on the burden of funding infrastructure improvements.

5. Thanks to rising foreign investment, competitiveness of the Spanish workforce has increased, yielding a high level of value-added production and increased automation. As a result, the risk of withdrawal of businesses and foreign investments may not be as high as once feared, easing the worries about negative aggregate effects on Spanish production and employment.

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OPPORTUNITIES  
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6. EU member countries have high expectations for the growth of their economies as a result of the EU enlargement. Spain, like its EU-15 counterparts, anticipates that the induction of the candidate countries will increase trade and investment. Most significantly, investment in infrastructure in the candidate countries will offer new prospects for large construction and high-tech infrastructure companies of the EU-15. For example, EU-15 companies have already successfully installed mobile phone networks in candidate states. The International Director of CEOE told us that Spanish companies are familiar with the EU contract process from years of completing EU-financed projects and should therefore have an advantage in bidding on infrastructure contracts.

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ACTION PLAN  
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17. According to the CEOE, as the inauguration date approaches, current member states should realize that EU enlargement is not a one-way process. Enlargement will require changes in both the candidate countries and the EU-15. If Spanish business leaders want to benefit from the opportunities while minimizing their exposure to risks, they need to specialize in products of high technology and value and focus on international markets. Spanish businesses should also adopt new technologies, foment Research and Development (R&D), develop human resources, improve infrastructure, and shape policies to attract foreign investment.

18. To reap benefits from enlargement, Spain will need to improve its business relations with the candidate countries. Spain's trade with Eastern Europe has increased in recent years, but business relations are weak compared with other EU member states. If Spain wants to penetrate these markets it should increase foreign direct investment in these countries. While Spanish presence in some sectors (like fisheries) will come easily, entry into many equally profitable sectors will require new business strategies.

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SECTORAL ANALYSIS  
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19. METAL INDUSTRY. This sector is especially sensitive to EU enlargement. The main concern is how cheaper imports of metals from candidate countries will affect the Spanish metal sector. Further, competition stemming from new members may affect Spain's share of the EU market. Spanish producers should focus on increasing their productivity by investing in R&D, increasing the product quality of their metals and relocating some production abroad.

10. AUTOMOBILE INDUSTRY. Currently, the majority of Spanish automobile production is exported to the EU-15. With a larger internal EU market after enlargement, there will be more sales prospects. However, Spanish auto producers will need to reduce costs as other auto-makers will take advantage of lower labor costs and fiscal incentives in the new member states while moving closer to larger markets of Central Europe. The relocation of production outside of Spain is already happening, as several car plants have relocated to Slovakia (reftel). However, high automation of automobile plants in Spain leads CEOE to predict that only 15% of the automotive workforce will be affected. At the same time, Spain may counterbalance some of the relocation of factories with its increasingly skilled workforce. Eventually, wages will converge, and with the final elimination of fiscal incentives, competition will be carried out on a more even playing field.

11. CONSUMER ELECTRONICS. Many multinational electronic producers have moved production abroad to lower wage locations to reduce production costs. To maintain its remaining electronics workforce, Spain will have to turn to higher value products by investing in R&D and making better use of its skilled workers-in short, increase productivity in this sector.

12. CHEMICALS. In the chemical industry, competition may arise from candidate countries that make primary materials for pharmaceuticals. Lower wages in candidate countries could also negatively affect the Spanish pharmaceutical industry. Spanish pharmaceuticals should venture into higher-value products by investing in R&D and taking advantage of the larger market. In regards to chemical products for industry and consumers, demand in the new markets will increase, providing prospects for higher-end Spanish products such as paints, detergents, fragrances and cosmetics.

13. TOURISM. Due to its strong position in world tourism, the Spanish tourist industry does not foresee any short-term adverse affects from EU enlargement. In the medium-term, candidate countries that have beaches and sun could take away some of Spain's market. In the long run, higher incomes of citizens of these countries will only benefit the Spanish tourism market. To attract these new customers, Spain will need to improve and diversify its services.

14. AGRICULTURE AND FOOD PRODUCTS. Spain will have to take into account that after the second phase of the integration process, the EU agricultural budget will be divided amongst twenty-five members. In the medium term, as Eastern European producers incorporate technology in their dairy and beef production, there will be tougher competition for Spanish producers. On the other hand, EU enlargement provides opportunities for the Mediterranean region.

Spanish agricultural producers should take advantage of the new markets where there is an increasing demand for processed food products rather than primary agricultural products.

15. FISHERIES. Spain's fishing industry produces more than twice the amount of the combined production of the ten candidate countries. In the short-run the new members will not be able to export fish products due to non-compliance with EU sanitary standards. Thus, the enlarged market can only have a positive impact on the Spanish fishing industry.

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COMMENT  
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16. In predicting a minor impact on Spanish GDP of plus or minus 0.3%, the CEOE is more optimistic about expansion than many observers. CEOE's report is unique in that it is the only one we have seen that offers specific advice to individual sectors on how to deal with the opportunities and challenges of expansion. Clearly, the degree to which Spanish businesses heed that advice will largely determine whether they gain or lose from enlargement.

ARGYROS